No. 11,643

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

BLOOMFIELD RANCH, by JAMES A. CLAYTON & Co., a corporation, managing partner, operator and co-owner thereof, and by FLORENCE G. BALDWIN, JOHN DERROL CHACE, WILLIS SHERMAN CLAYTON, JR., ARTHUR D. CURTNER, JOHN KIRK DORRANCE, ROSE L. FITCH, MARGARET F. COYKENDALL, HUGH S. HERSMAN, ALFRED A. HAPGOOD, GEORGE H. OSEN, ALFRED L. PARKINSON, ESTATE OF ANDREW R. PATRICK, deceased, by SIGURD C. P. CORNETT, as executor of the will of Andrew R. Patrick, deceased, SAN JOSE HARDWARE Co., a corporation, NELLIE SHILLINGSBURG, ANNE THOMPSON, SARAH SHILLINGSBURG BARRY, MARGARET LEAMAN, and ESTATE OF ELLEN WEINSTEIN, deceased, by WELLS FARGO BANK & UNION TRUST Co., executor, substituted for Estate of Samuel Weinstein, deceased, by Ellen Weinstein, as executrix of the will of Samuel Weinstein, deceased, partners in and co-owners of Bloomfield Ranch,

Petitioners on Review,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent on Review.

On Petition for Review of Decision of the Tax Court of the United States.

PETITIONERS' PETITION FOR A REHEARING.

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Codes

Miscellaneous

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To the Honorable Francis A. Garrecht, Presiding Judge, and to the Honorable Associate Judges of the United States Circuit Court of Appeals for the Ninth Circuit:

The petitioners in the above-entitled case respectfully petition for a rehearing upon the following grounds:

1. The Court has determined, as we understand the opinion, that the taxpayers constituted a code association taxable as a corporation and were not a code partnership by applying as the determinative test lack or existence of intentional joint activity or endeavor. The decision rests on the application of that test to the facts of this case. This test, it seems to us, is not recognized by statutes, decisions or regulations and is contrary to Internal Revenue Code, Sections 3797(a)(2) and (3), and the regulations issued pursuant thereto. Furthermore, this test is in conflict with the applicable decisions of the Supreme Court and of the Circuit Courts of Appeals in other circuits. Among such decisions we cite:

Morrissey v. Commissioner, 296 U. S. 344;
Commissioner v. Rector & Davidson, C.C.A. 5, 111 Fed. (2d) 332;
Burnet v. Burns, C.C.A. 8, 63 Fed. (2d) 313;
Commissioner v. Whitcomb, C.C.A. 5, 95 Fed. (2d) 596;
Lewis & Co. v. Commissioner, 301 U. S. 385.

The test of an association taxable as a corporation as laid down in the *Morrissey* case is not lack or existence of intentional joint activity or endeavor but

rather whether the parties involved are engaged (1) in carrying on business, and, if so, (2) in the form and manner of a corporation. The application of the test laid down by the Court here, it seems to us, is a denial of the test laid down in the *Morrissey* case.

2. The Court holds that there was no joint activity on the part of the Bloomfield taxpayers but that a partnership or joint venture implies an association and entering into a joint enterprise. The Court says further that a partnership or joint venture conceives the intentional combination and joint endeavor of the parties interested in the common enterprise for their mutual benefit, and not merely the appearance of combination or collective action by accident. After distinguishing between a joint venture and a partnership (a joint venture is a form of partnership under the code definition) the Court adds that the element of collective and conjunctive action for the mutual benefit of all engaged therein is necessary in both a partnership and a joint venture; that is in those two forms of code *partnership.*

On this ground the Court holds that the taxpayers here did not constitute a code partnership.

In explaining this position the Court says: "We do not think that the federal courts in decisions involving the identity of an organization as a partnership under the Internal Revenue Code have willfully ignored or denied the basic concepts of a partnership under general principles of law." That, as we understand the opinion, is to say that a code partnership must have

the characteristic elements of a common law partnership.

Lack or existence of intentional joint activity or endeavor is not a test of *distinction between* code partnerships and code corporations or associations because there can be code partnerships with or without such joint activity or endeavor but there cannot be a code association or corporation without it. The Attorney General in his brief in this case based his position on the contention that the taxpayers "joined in a common enterprise" (p. 15) and were "jointly investing capital in a common enterprise with a view to sharing its profits." (p. 16.) Otherwise he would have been compelled to concede that the taxpayers were not an association taxable as a corporation. The effect of the Court's opinion is to negative that contention of the Attorney General, for he evidently has in mind *intentional* participation in a joint enterprise. The Bloomfield taxpayers *intended* to do what they did. If what they did makes them an association of any kind, it was an association intended by them. If it was not, then they cannot be taxed as an association or code corporation.

The Court quotes the *Morrissey* case (296 U. S. 344) to the effect that an association has been defined "to imply associates and entering into a joint enterprise". The Supreme Court's reference to an association in that quotation is not to a partnership or joint venture but to a code association taxable as a corporation—"the statutory concept of 'association' " as the Court there says. No distinction between in-

tentional joint action and "the appearance of combination or collective action by accident" is made by the *Morrissey* case decision. There must be some form of joint action to constitute either a code partnership or a code association taxable as a corporation. If there was in the Bloomfield case no joint activity (and this is what the Court here holds), then there was no association acting under the semblance of a corporation and therefore no association taxable as such.

In short the ground on which the Court bases its holding that Bloomfield Ranch was not a code partnership forbids the conclusion that it was a code association or corporation, and indicates a conclusion that it was merely a group of individuals acting through a common agent, which was precisely the position which the taxpayers here have taken. Such a group is within the *code definition* of partnership, but not within the code definition of corporation or association doing business in the way of a corporation. The joint action in the Bloomfield enterprise is that all the investors, being co-tenants, chose the same agent.

The *Tower* case (327 U. S. 280-286) on which this Court relies to support the distinction made does not deal with the difference between a code "association" and a code "partnership". Tower and his wife claimed that they were ordinary or common law partners and that, as such, each was required to report only his distributive share of the ordinary net income of the partnership. The Commissioner contended *not* that

they constituted a corporation or association, but that Tower as an *individual* was the owner and operator of the business and that the wife was not a partner at all, and that her alleged membership was a sham, so that the entire income was taxable to Tower alone. The language from the *Tower* case quoted in the opinion in this Bloomfield case defined and was concerned with a common law partnership solely, and is not authority for the precept that the element of collective and conjunctive action, intentional or otherwise, for the mutual benefit of all engaged therein is necessary in a *code* partnership. Nor does it tend to sustain a conclusion that intentional collective and conjunctive action is an essential element of a code partnership but not of a code association taxable as a corporation. We are aware of no authority, and none is cited in the opinion, holding that the presence or absence of "intentional joint action and combination of effort in the undertaking" is a mark of the *difference between* a code partnership and a code association or corporation.

We do not find in reading the opinion in the *Gerstle* case that the Court there stressed (as the opinion here says it did) the importance of intentional joint action and combination of effort or even mentioned such as a reason for holding the Gerstle syndicates to be code partnerships. The excerpts from the *Gerstle* case quoted in that connection are nothing more than a recital of fact showing what was done by the syndicate members in that case. The Court there pointed out that, while title was not taken in the syndicate

managers, continuity of the enterprise and centralized management existed "*notwithstanding* in practice there was general consultation before important decisions were reached." The decision was based on the lack of certain characteristic advantages of corporate organization there mentioned and specifically listed in taxpayer's opening brief in the Bloomfield case at pages 46 to 53.

3. The Court, it seems to us, has not given sufficient heed to the difference between the definition of a partnership recognized prior to the change by the 1932 Revenue Act and the changed definition which provided its own concept of partnership and discarded common law tests. Prior to the 1932 Act the term "partnership" was held to mean a partnership under general law. As a result, syndicates, groups, pools, joint ventures and similar organizations were not required to file income tax returns. The 1932 Act included these organizations within the meaning of partnership. In pointing out the confusion which theretofore existed with respect to such returns the Ways and Means Committee of the House of Representatives in its report on the 1932 Revenue Act (72nd Congress, First Session, House Report 708 at page 53) stated:

> "The Bill does away with this uncertainty by placing all joint ventures, syndicates, pools and similar organizations which do not constitute associations or trusts, in the category of partnerships, and the members of such syndicates, pools, etc., in the category of partners. This provision

> will have the effect of requiring the syndicate to file an information return similar to the return of a partnership and will thus make it easier for the members to determine the distributive shares in the syndicate gains and losses which are to be included in their own returns."

It is obvious, therefore, that the purpose of this change in the definition of partnership (first enacted in the 1932 Revenue Act and continued from that time into the Internal Revenue Code) was to treat as partnerships business organizations which in fact were not partnerships under general law. In fact, a reading of the Internal Revenue Code, Section 3797(a)(2) shows that the term "partnership" is used to include all business organizations, which are not, within the meaning of the code, a trust, estate or corporation. The Court in its opinion here seems to say that because Bloomfield Ranch lacks an element of a true partnership it must be an association taxable as a corporation. This, we respectfully suggest, is clearly erroneous. The code provides that an organization which is not a trust, estate or corporation is a partnership. We demonstrated in our briefs that Bloomfield Ranch lacked the elements of a corporation or of an association. This Court found Bloomfield Ranch lacked the essential element of an association, namely, joint activity. Therefore it must follow that Bloomfield Ranch is classified as a partnership under the Internal Revenue Code, that is as a group, syndicate, pool, or joint venture, since Bloomfield Ranch cannot be classified as a trust, estate, or corporation.

4. The Court says that it has considered the lack of interrelation between the taxpayers here and has noted it as an element of dissimilarity between this and the *Gerstle* case, but, as we have indicated, this element of dissimilarity is a distinction without a difference.

The application by the Court in this case to the Bloomfield taxpayers of the five standards or tests to characterize a code corporation listed in the *Morrissey* case will fit the *Gerstle* case just as aptly. In the taxpayers' opening brief (pages 46 to 53) we listed the points of *analogy* between the Bloomfield case and the *Gerstle* case and we shall not repeat them here, but the Court's opinion here mentions no point of *difference* except lack of interrelation between the taxpayers in the Bloomfield case.

5. The opinion holds that the acts of Clayton & Co. were not performed as an agent. It does not suggest the capacity in which Clayton & Co. did perform those acts or could have performed them if not as agent. To say as the opinion does that "the operator, no doubt, was *in a sense* the representative of the Investors in carrying on the plan" seems to us inconsistent with the statement that it was not an agent. Manifestly Clayton & Co. was not a trustee, since it did not hold the title. The fact that the Operator, as the opinion says, "could and did act independently of the Investors pursuant to the needs of the moment and its acts in that respect were beyond their control" does not make the operator any more or less than an agent with plenary authority, but still an agent.

6. The Court held that Investors "were not given any undivided interest in the realty". We respectfully submit that under the law of California, which law must govern this question, the Investors, by operation of law, acquired undivided interests in the realty at the time of its purchase by Clayton & Co. on their behalf. There was no need for any one to give to the Investors, nor for the Operator or for Thomas to convey to them, any interest in the property. Their interest vested at the time of the conveyance from Miller & Lux to Thomas. See our opening brief, pages 23 to 26. For that reason, we submit, the Court has decided an important question of local law in a way in conflict with applicable state decisions.

The Investors were the owners of an undivided interest in realty as tenants in common. Each of them appointed Clayton & Co. to be his agent with respect to his interest in that property. Since there was no other joint activity on their part (and the Court here so found) they could not constitute a code association or corporation since under the Internal Revenue Code they were not a trust, not an estate, not a corporation, and under Section 3797(a)(2) they did constitute a partnership; that is, a group, syndicate, pool or joint venture.

Not only in the *Gerstle* case but in the following cases cited and quoted in our opening brief co-tenants of real property who had transferred the bare legal title to a trustee for convenience and who conducted the enterprise acting through a common agent (as in this case and the *Gerstle* case) were said to con-

stitute a joint venture or code partnership and not a trust or estate or a corporation.

Commissioner v. Rector & Davidson (C.C.A. 5, 1940), 111 F. (2d) 332;

C. A. Everts, et al., v. Commissioner (1938), 38 B.T.A. 1039;

C. H. Clovis (1935), 32 B.T.A. 646;

Stantex Petroleum Co., Trustee (1938), 38 B.T.A. 269.

While in *Lewis v. Commissioner* (1937), 301 U. S. 385, there was only one owner, the principle and language of the opinion are applicable here.

The circumstances that in some of those cases the Investors signed an agreement with one another as well as with the common agent whereas the Bloomfield Investors severally signed an agreement only with the agent is an element of strength (not, as the Court's opinion suggests, of weakness) in our contention that the Bloomfield Investors were not a code association or corporation because here there was no joint agreement but only appointment of a common agent and nothing analogous to a corporate board of directors directing the agent.

Dated, San Francisco,
May 20, 1948.

O. K. Cushing,
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CERTIFICATE OF COUNSEL.

The undersigned counsel for petitioners hereby certify that in their judgment the foregoing petition for a rehearing is well founded and that it is not interposed for delay.

Dated, San Francisco,
May 20, 1948.

O. K. CUSHING,
DELGER TROWBRIDGE,
EUSTACE CULLINAN,
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